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In the Supreme Court of the United States

OCTOBER TERM, 1942

No. 846

MAGNUS BECK BREWING COMPANY, INC., PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 23–27) is reported in 46 B. T. A. 78. The opinion of the Circuit Court of Appeals (R. 44–47) is reported in 132 F. (2d) 379.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on December 23, 1942 (R. 47–48). The petition for a writ of certiorari was filed on March 23, 1943. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial

Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether a contract requiring the taxpayer corporation to pay to a trustee for its creditors a stated amount upon each barrel of beer sold by it during each week, is a contract which "expressly deals with the disposition of earnings and profits of the taxable year" within the meaning of Section 26 (c) (2) of the Revenue Act of 1936.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved may be found in the Appendix, *infra,* pp. 7–9.

STATEMENT

Pursuant to a trust agreement dated January 31, 1934 (R. 10–17), the taxpayer, Magnus Beck Brewing Company, Inc., obligated itself to pay to a designated trustee "Fifty cents (50¢) per barrel on all beer sold during the months of April and May, 1934, and One Dollar ($1.00) per barrel on all beer sold thereafter." (R. 12–13.) The fund so created was to be paid to specified creditors in accordance with an agreed plan of priorities. (R. 14.) The trustee was given power to "waive" the prescribed payments "if he shall deem such waiver expedient and necessary." (R. 13.) In the event of a continued default the trustee was empowered to foreclose the mortgage which had been given as security for performance. (R. 13.) The taxpayer had an oral understand-

ing with the trustee that it should pay its indebtedness from earnings. (R. 25.)

In 1936, the tax year in question, the taxpayer sold 64,746.75 barrels of beer and paid $47,332.98 to the trustee. (R. 25.) In that year its profits totalled $60,415.96. (R. 26.)

In computing the surtax on undistributed profits imposed by the Revenue Act of 1936, the taxpayer claimed and the Commissioner of Internal Revenue denied a credit of $47,332.98 under Section 26 (c) (2). (R. 26.) The issue presented was whether the trust agreement in question contained a provision which "expressly deals with the disposition of earnings and profits of the taxable year" within the meaning of that section. The Board of Tax Appeals answered this question in the affirmative and, therefore, concluded that the contested deduction should have been allowed. (R. 27.) The Circuit Court of Appeals for the Second Circuit answered the question in the negative and reversed. (R. 47.)

ARGUMENT

The trust indenture did not expressly provide that the specified payments be made out of or be measured by the earnings and profits of the taxable year. Although the taxpayer's payments to the trustee in 1936 were made out of its 1936 earnings, this was not a legal requirement of the trust indenture. A contractual requirement of this nature is not one which "expressly deals with the

disposition of earnings and profits of the taxable year," as the statute (Section 26 (c) (2)) specifically requires. Cf. *Helvering* v. *Maloney Electric Co.*, 120 F. (2d) 617, 620 (C. C. A. 8), certiorari denied, 314 U. S. 682, rehearing denied, 315 U. S. 826; *C. C. Clark, Inc.* v. *United States*, 126 F. (2d) 292, 294 (C. C. A. 5); *Nevada-Massachusetts Co.* v. *Commissioner*, 128 F. (2d) 347 (C. C. A. 9); *Clover Splint Coal Co.* v. *Commissioner*, 130 F. (2d) 52 (C. C. A. 3); *Commissioner* v. *Saginaw & Manistee Lumber Co.* (C. C. A. 7), decided February 27, 1943 (1943 Prentice-Hall Federal Tax Service, par. 62,531). Accordingly, the court below, in accordance with the virtually unanimous court decisions, correctly rejected the contention, that the deduction was nevertheless available because as a practical matter the circumstances were such that the payments could only be made out of earnings and profits.

The only decision which looks the other way is *Commissioner* v. *Michigan Silica Co.*, 124 F. (2d) 397 (C. C. A. 6).[1] This decision has not been followed in the other circuit courts of appeals, and

[1] Petitioner contends (Pet. 6) that *Clover Splint Coal Co.* v. *Commissioner*, *supra*, likewise is contrary to the decision below. However, the explanation offered (Pet. 13) in support of this contention discloses that petitioner means only that the instant problem was not considered in that case and therefore may be an open one in the Third Circuit. The contention even thus qualified is of dubious merit.

would in all probability no longer be considered controlling in the Sixth Circuit. It was a memorandum decision which concluded by citing *Commissioner* v. *Strong Mfg. Co.,* 124 F. (2d) 360, decided the same day by that same court. The rationale of the two decisions is the same, namely that practical effect on the taxpayer rather than precise contractual language is the controlling test in applying Section 26 (c) (2). Since that rationale was rejected by this Court when the *Strong Mfg.* case, together with its companion cases,[2] was reversed (*Helvering* v. *Ohio Leather Co.,* 317 U. S. 102), the *Michigan Silica* case is probably no longer authoritative in the Sixth Circuit. This conclusion is fortified by the fact that this Court expressly pointed out (*Helvering* v. *Ohio Leather Co.,* 317 U. S. 102, 106–107) that one of the conditions precedent to the allowance of a credit under Section 26 (c) (2) is the existence of a contractual provision (absent both here and in the *Michigan Silica* case) expressly dealing with the disposition of earnings and profits.

The problem is not one of present importance[3] and in the absence of a clear existing conflict of decisions we believe that review by this Court is not warranted.

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[2] *Commissioner* v. *Ohio Leather Co.,* 124 F. (2d) 397; *Commissioner* v. *Warren Tool Corp.,* 124 F. (2d) 397.

[3] It arises only under the Revenue Act of 1936. Cf. Section 27 (a) (4) of the Revenue Act of 1938; Section 27 (a) (4) of the Internal Revenue Code.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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